Natural Sciences and Engineering Research Council of Canada Quarterly Financial Report for the Quarter Ended June 30, 2013

Statement Outlining Results, Risks and Significant Changes in Operations, Personnel and Programs

1. Introduction

The Natural Sciences and Engineering Research Council of Canada (NSERC) was established in 1978 by the *Natural Sciences and Engineering Research Council Act*, and is a departmental corporation named in Schedule II of the *Financial Administration Act*. NSERC's purpose is to help make Canada a country of discoverers and innovators for the benefit of all Canadians, by supporting postsecondary students and postdoctoral fellows in their advanced studies, promoting discovery by funding the research programs of academic researchers, and stimulating partnerships between academia and industry. Further information on the NSERC mandate and program activities can be found in Part II of the Main Estimates.

This Quarterly Financial Report (QFR) has been prepared by management as required by section 65.1 of the *Financial Administration Act* and in the form and manner prescribed by the Treasury Board. This quarterly report should be read in conjunction with the Main Estimates and Supplementary Estimates for 2013-14.

Basis of Presentation

This quarterly report has been prepared by management using an expenditure basis of accounting. The accompanying Statement of Authorities includes NSERC's spending authorities granted by Parliament and those used by the department, consistent with the Main Estimates and Supplementary Estimates for the 2013-14 fiscal year. This quarterly report has been prepared using a special purpose financial reporting framework designed to meet financial information needs with respect to the use of spending authorities.

The authority of Parliament is required before monies can be spent by the Government. Approvals are given in the form of annually approved limits through appropriation acts or through legislation in the form of statutory spending authorities for specific purposes.

As part of the parliamentary business of supply, the Main Estimates must be tabled in Parliament on or before March 1 preceding the new fiscal year. Budget 2012 was tabled in Parliament on March 29, after the tabling of the Main Estimates on February 28, 2012. As a result, the measures announced in Budget 2012 could not be reflected in the 2012-13 Main Estimates.

In fiscal year 2012-13, frozen allotments were established by Treasury Board authority in departmental votes to prohibit the spending of funds already identified as savings measures in Budget 2012. In 2013-14, the changes to departmental authorities were reflected in the 2013-14 Main Estimates tabled in Parliament.

When Parliament is dissolved for the purposes of a general election, section 30 of the *Financial Administration Act* authorizes the Governor General, under certain conditions, to issue a special

warrant authorizing the Government to withdraw funds from the Consolidated Revenue Fund. A special warrant is deemed to be an appropriation for the fiscal year in which it is issued.

NSERC uses the full accrual method of accounting to prepare and present its annual departmental financial statements that are part of the departmental performance reporting process. However, the spending authorities voted by Parliament remain on an expenditure basis.

This quarterly report has not been subject to an external audit or review.

2. Highlights of Fiscal Quarter

Statement of Authorities

Available Authorities

As of June 30, 2013, NSERC's total available authorities for 2013-14 amount to $1,050 million. The changes in available authorities are the result of previous federal budget announcements that impact both the operating authorities (vote 75), and the grants and scholarships program authorities (vote 80) in the current fiscal year. To date, for 2013-14, these changes resulted in a decrease in total authorities of $7 million (0.7%) over the prior year, of which $4.8 million (69% of the total changes) represented a decrease in NSERC's grants and scholarships programs while the authorities for operating and employee benefits expenditures decreased by $2.2 million.

In this quarter, total available authorities incorporate the elements of the 2013-14 Supplementary Estimates (A) (SEA). The SEA is the first of three opportunities to approve changes in NSERC's authority levels for the current fiscal year (other than transfers from Treasury Board votes). The vast majority of these changed elements are the result of previous federal budget announcements, while the balance relates to technical adjustments from Treasury Board and transfers between departments and agencies for specific initiatives. The future and ongoing impacts of SEA elements will be included in NSERC's 2014-15 Main Estimates for the next fiscal year. For the ongoing elements from previous federal budget announcements or transfers between departments and agencies, only the net difference in the level of funding between the two fiscal years is presented in the explanation below. The net changes, amounting to the $7 million decrease in total available authorities between the current and previous fiscal year, comprise of the following elements:

- an increase of **$15.0 million** in the Research Partnerships Program to support the Strategy for Partnerships and Innovation to increase innovation and industrial investment in R&D in Canada (Budget 2012);
- an increase of **$9.3 million** in the Business-Led Networks of Centres of Excellence program to make the program permanent as part of an initiative to link innovative businesses to Canada's world-class researchers, helping to create and sustain knowledge-based jobs (Budget 2012);
- an increase of **$7.0 million** in the Industrial R&D Internship program to make the program permanent as part of an initiative to link innovative businesses with students to support the entrepreneurial advantage (Budget 2007);
- an increase of **$4.7 million** for the Centres of Excellence for Commercialization and Research program to create a more effective and efficient way to identify commercialization opportunities (Budget 2007);

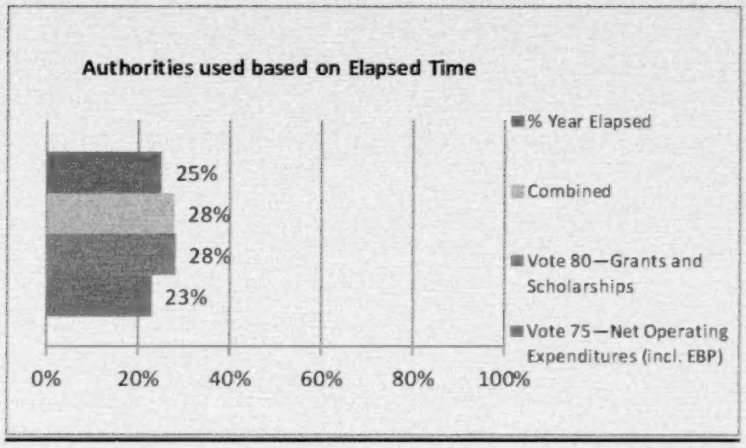
- an increase of **$1.0 million** in the ramp up of funding to the College and Community Innovation program (Budget 2011);
- an increase of **$0.7 million** as part of the collective bargaining agreement;
- an increase of **$0.3 million** due to a timing difference for net grant transfers between federal departments made to National Defence to support the Canada Research Chairs of federally-funded academic research at the Royal Military College;
- a decrease of **$30.0 million** as part of the Deficit Reduction Action Plan initiative to find efficiencies and reduce government spending (Budget 2012);
- a decrease of **$14.0 million** for the Canadian Light Source initiative due to the sunsetting of the program (Budget 2008);
- a decrease of **$0.9 million** in the Networks of Centres of Excellence program to support the Canada-India Research Centre of Excellence initiative that falls under the health research mandate; and
- a decrease of **$0.1 million** in the Networks of Centres of Excellence program to support the Canada-India Research Centre of Excellence initiative that falls under the social sciences and humanities mandate.

Authorities Used in the First Quarter

This departmental QFR reflects the results of the current fiscal period in relation to the 2013-14 Main Estimates and the Supplementary Estimates (A), for which full supply was released by Parliament on June 20, 2013.

The total authorities used during the first quarter of 2013-14 amounted to $291 million (28% of the total available authorities; 28% of total authorities used for grants and scholarships programs and 23% for operating expenditures and employee benefits). The expenditures are $8.8 million more than at the end of the same quarter in the previous fiscal year. This increase is principally related to grants and scholarships programs. The increase in grants and scholarship expenditures is the net result of the previously expanded program authorities in specific programs, increasing demand in some programs, and payment timing differences between the first and second quarters of the comparative fiscal years, which are expected to offset by year-end.

Grants and scholarships payments vary between periods due to the cycle and results of the peer-reviewed program competitions, and the multi-year award profiles. The operating expenditures cover personnel and other operating expenses required to support the delivery of the grants and scholarships programs. Expenditures related to the Employee Benefit Plan are accounted for separately in statutory authorities. Although the majority of personnel expenditures and other operating costs are incurred in a consistent manner throughout the fiscal year, the balance of expenditures, including temporary employees hired for the peak competition season and travel costs for peer reviewers, occur in direct conjunction with the program cycle and are demand driven. As a large proportion of the program competitions occur in the final quarter of the fiscal year, the operating expenditures in each of the first three quarters are typically less than 25% of the annual operating available authorities.



Statement of Departmental Budgetary Expenditures by Standard Object

Variation in Amounts Available for Use in 2013-14

As described in the Available Authorities section, NSERC's Parliamentary authorities have been decreased by $7 million for 2013-14 to date over the prior year, the bulk of which is attributed to the decrease in authorities for transfer payment programs ($4.8 million).

Transfer Payments Expenditures (Grants and Scholarships)

First Quarter Grants and Scholarships Expenditures

Transfer payments represent approximately 95.5% of NSERC's available authorities. Variations occur in transfer payment expenditures between quarters due to the nature of program cycles. During the first quarter of 2013-14, NSERC's actual transfer payment expenditures have increased by $8.7 million compared to the same quarter of the previous fiscal year. There was a number of differences in specific programs from year to year:

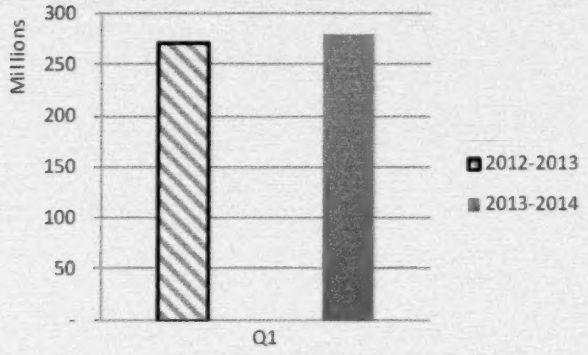
- An increase of $3.2 million over the previous year related to some expanded program authorities and the related increased take-up in certain programs in the first quarter for the programs part of the Strategy for Partnerships and Innovation ($1.8 million in Collaborative Research and Development Grants and $1.4 million in Engage Grants).
- The Collaborative Research and Training Experience Program (CREATE) experienced an increase of $2.6 million from last year. This year, the number of new applications increased by 15 which represents an expected increase of $5 million in expenditures in this program by the end of current fiscal year. This factor combined with a timing difference on payments in 2012-13 due to diligence analysis of the mid-term reviews, which resulted in awards not being released at the same time or being cancelled entirely explained the increase in spending over the last fiscal year.
- An increase of over $4 million mainly due to timing differences on payments for the Centres of Excellence for Commercialization and Research Program ($1 million), the Industrial R&D Internship Program ($1.6 million) and Networks of Centres of Excellence ($1.4 million).

- An increase of $2.5 million explained by the ramp-up of the Collaborative Health Research Program due to the shifting of priorities.

- A decrease of $2.7 million in the University-Industry-Project mainly due a payment timing difference on the Auto Partnership Program.

- A decrease of $0.9 million in the Strategic Network Grants Program explained by a ramp-down of the program due to the shifting of priorities.

Grants and Scholarships Expenditures Trend



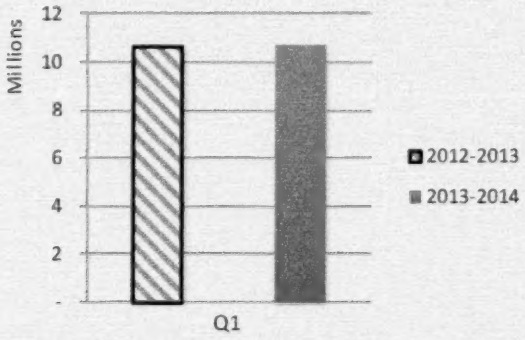
Personnel Expenditures

Personnel expenditures in support of program delivery account for the largest proportion of NSERC's planned operating expenditures (over 73% of available operating authorities and planned operating expenditures for 2013-14). The personnel expenditures for the first quarter of 2013-14 are generally in line with the comparable expenditures of the prior year.

Non-Personnel Operating Expenditures

Non-personnel operating expenditures include all other operating costs related to the support of program delivery, a significant proportion of which relates to program competitions that take place predominantly during the latter quarter of the fiscal year. The non-personnel operating expenditures for the first quarter of 2013-14 are generally in line with the comparable expenditures of the prior year.

Operating Expenditures Trend



3. Risks and Uncertainties

Funding and Program Delivery Risk Factors

Through the Council's most recent corporate risk identification exercise, the risks that have a potential financial impact or that deal with financial sustainability have been assessed. The impact on NSERC and the planned mitigation strategies related to these risks are discussed below.

External Risk Factors

NSERC is funded through annual parliamentary spending authorities and statutory authorities for program transfer payments (grants and scholarships programs) and its supporting operating expenditures. As a result, its program activities and operations are impacted by any changes to funding approved through Parliament. Accordingly, delivering programs can be affected by factors such as the economic and political climate, technological and scientific development, and evolving government priorities, which impact approved resource levels (total available authorities).

Research and innovation are part of global trends; therefore participation in our programs is not only influenced by the Canadian context, but also by initiatives and opportunities worldwide. Formal communications and external relation strategies are developed by NSERC to ensure that stakeholder relationships and expectations are managed effectively and that NSERC has fulfilled the research and innovation needs.

There is also the risk that NSERC fails to achieve its mandate and strategic outcomes. To mitigate this risk, an integrated planning process was launched by NSERC in 2012. This process will serve as the foundation for NSERC to plan all aspects of its business in an integrated manner and, to align priorities and resources accordingly.

Internal Risk Factors

NSERC is a knowledge-based organization that relies on maintaining its talented and committed workforce to deliver its programs. To retain its valuable human resources and their corporate memory, NSERC is developing a human resources strategy that outlines the organization's commitments and action plan for developing talent and for building and sustaining a thriving and successful workplace and work culture. NSERC's financial restraints are challenging the ability to hire the skilled resources needed to successfully achieve the transformation and realignment agendas to meet tomorrow's needs. Potential consequences could include workload management issues and succession planning challenges.

NSERC is transforming its business in order to adapt more efficiently to internal changes and to improve external client service.

The budgetary pressures have required internal reductions and reallocation measures. These pressures are compounded by the operational requirement to support an increased and broadened program base while processing an increasing number of applications and absorbing inflationary costs on operating expenditures within limited or decreasing operational envelopes. NSERC is also managing the requirement for the implementation of modernized technology solutions to better support program delivery.

Thus far, NSERC has achieved the reduction of its operating pressures through economies of scale achieved by the shared administrative service arrangements with the Social Sciences and Humanities Research Council of Canada (SSHRC), corporate-wide prioritization and harmonization or reduction of activities, internal reallocations, and a focus on streamlining and generating efficiencies wherever possible. An established budgetary process with regular in-year budget reviews and formal reallocations for emerging priorities approved by senior management supports this endeavour. NSERC is also undertaking a revision of its operating and grant delivery systems and processes to generate further efficiencies and future savings.

NSERC is a lean agency in terms of operating funding provided to deliver existing and expanding programs (less than 5% of total resources). NSERC is pursuing business transformation to address restraint measures and funding cuts, and to enhance resource decision-making.

4. Significant Changes Related to Operations, Personnel and Programs

There were a number of important changes in comparison with the previous fiscal year that relate to operations, personnel and programs. These include the impacts generated by NSERC's previously increased available authorities, which resulted in expanded Strategy for Partnerships and Innovation program dimensions. Another prevalent influence involved the continuing implementation of government-wide operating budget constraint measures and the government's efforts to return to a balanced budget, for which details are described in the section below. The federal Budget 2013, tabled in March, included funding announcements with additional program dimensions that are being implemented by NSERC, following Treasury Board and Parliament approvals, over the course of the fiscal year.

5. Budget 2012 Implementation

This section provides an overview of the savings measures announced in Budget 2012 that are being implemented in order to refocus government and programs; make it easier for Canadians and business to deal with their government; and, modernize and reduce the back office.

Through the Economic Action Plan 2012, NSERC has achieved savings of approximately $30 million in 2013-14 and ongoing. Over Budget 2012 and Budget 2013, the Government of Canada reinvested $30 million, annually on an ongoing basis, in support of the Strategy for Partnerships and Innovation, making the net impact on NSERC's overall budget neutral for 2013-14.

NSERC examined all of its activities and investments, with the intention of streamlining operations and ensuring maximum efficiencies.

In realizing operating budget savings, a number of measures are being implemented to generate greater efficiency and effectiveness, including an enhanced use of technological advancements, such as teleconferencing and virtual meetings. A rigorous and cohesive approach to priority setting, project planning and training will further help the Council meet its goals.

Expenditures in the first quarter of 2013-14 are higher than in the same period from the previous fiscal year. The difference between the two fiscal years is due to timing differences in payments at this stage and increases in take-up in some programs. The operating expenditures have generally remained the same as in the comparable period of the prior year, which reflects savings equivalent to the inflationary pressures.

There was no incremental funding provided to NSERC to implement the cost savings measures.

There are no specific financial risks or uncertainties related to these savings.

Approved by:

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August 14, 2013